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SUBJECT: CANADA: NEW BUDGET COULD SPUR FEDERAL ELECTION

Summary

¶1. (SBU) Canada's Conservative Government will deliver its second federal budget on March 19. The budget vote, possibly as early as the week of March 26, is an automatic confidence vote that could determine the timing of the next federal election. The budget will be seen as a sign of the Harper Government's intentions on election timing: as the springboard into an early election or the basis of a more polished platform for a fall vote, or even a 2008 election. The release of the budget is the opening dance of an election three-step of the federal budget, the Quebec provincial election on March 26, and a possible spring election call. Although the timing of the election is not yet a foregone conclusion, until the matter is resolved the government will be distracted and progress on major bilateral initiatives is effectively on hold. End summary.

Confidence Motion

¶2. (SBU) The House of Commons returns on March 19 for a two-week sitting before it breaks for Easter. The Senate returns on March 20. The federal 2007 budget will be the centerpiece and the test of the Conservatives and the opposition parties, willingness to go to the polls. A maximum of four days are allotted to debate on the budget motion with March 20 and 21 already slated for days one and two of debate, and the remaining two days expected to be allotted during the following week.

¶3. (SBU) The first of several votes on supplementary estimates will also come on March 22, possibly providing an early test of the mood of the opposition parties. As the official opposition, in this case the Liberals, usually votes against the budget on principle, the minority Conservative Government will require the support of at least one of the two smaller parties in the House of Commons. Current party standings are: Conservatives 125, Liberals 101, Bloc 50, NDP 29, Independent one, vacant 2. So far, it appears no deal has been reached in advance with any of the opposition parties regarding the budget. Thus, even more than usual, the budget will be a highly political document.

Winning Budget

¶4. (SBU) Government sources say that the budget has been carefully calibrated to appeal to the opposition, but it has also been crafted to win a second mandate. If it is defeated, the budget will be the focus of what the Conservatives hope will be a saleable, pragmatic package of lower taxes, less intrusion into provincial jurisdiction,

more law and order, and improved national security. Policy is likely to be secondary to the short-term expedient of sealing a majority government for the Conservatives. Current estimates suggest the Harper Government may have as much as C\$7-10 billion in surplus cash to divide between programs, tax cuts and debt repayment in the 2007 budget.

¶5. (SBU) The Harper Government has already telegraphed certain elements of the budget in advance: tax cuts, income-splitting for seniors, plans to settle the so-called federal-provincial "fiscal imbalance," increases to military and health funding as outlined in last year's budget, spending on the environment and agriculture, debt repayment, child care, and formalization of changes to taxation of income trusts. Of these, most attention will be on taxes, the fiscal imbalance, and the environment. The Conservatives have floated a "tax-back guarantee" that would reinvest interest savings from the national debt in personal tax cuts.

They may also raise the lowest tax threshold to provide relief for the working poor and the middle class, and, possibly, enrich child tax benefits aimed at lifting children and low-income working families out of poverty. Also possible is a cut in capital gains taxes on investments. The tax cuts are likely to be announced with fanfare, but in practical terms may not amount to more than C\$200 per year for the average taxpayer. Few changes are expected to corporate taxes.

Provincial Play

¶6. (SBU) Settlement of the fiscal imbalance will address the Prime Minister's 2006 election promise to Quebec, which is expected to be the primary beneficiary of the deal, and try to buy peace with all the provinces through significant per capita transfers for postsecondary education and

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infrastructure as part of reform of the formula for equalization. The deal is already a factor in the current Quebec provincial election campaign that ends on March 26. The incumbent federalist Liberal Party of Quebec under provincial Premier Charest is using it to trumpet the rewards of co-operative federalism and the benefits of remaining in Canada.

¶7. (SBU) If the cash is enough to salvage the Quebec Liberal Government, even a minority one, from an exceedingly tight three-way race, the federal Conservatives also hope that the deal would boost their own fortunes in the province. The Conservatives will argue that they have delivered on their commitment to recognize the fiscal imbalance and reduce and realign the federal role in areas of provincial responsibility. Mr. Harper captured ten seats in Quebec on the strength of that pledge and hopes to get more support from Quebecers in his second bid to win a majority government. However, current polls in Quebec suggest that the province may well elect its first minority government since 1878, a barometer of public opinion that could halt the rush to a federal election.

Eco-Appeal

¶8. (SBU) New spending on the environment is also likely calculated to appeal to the growing number of Canadians, and Quebecers in particular, who identify the environment as a key issue of concern. In the past few weeks, the Harper Government announced almost \$2 billion for green projects under the rubrics ecoTrust to fund provincial projects to reduce greenhouse gas emissions and air pollutants and ecoEnergy focused on efficiency, conservation, and cleaner energy and additional grants for mass transit to convince the Canadian public of his government's "green credentials."

¶9. (SBU) If the Liberals are the only party to oppose the budget, the confidence vote attached to it will be an

anti-climax. Only the Bloc has a clear bottom line, making its support dependent on "significantly" addressing the fiscal imbalance. Tax cuts for families and environmental spending would also be sweeteners. Support for the Bloc in Quebec remains well below its high of about 49% from the 2004 federal election and, if its provincial cousin the PQ does poorly in the March 26 Quebec provincial election, the Bloc will be even less tempted to provoke an election in which it could lose seats.

¶10. (SBU) The NDP is a wild card. It has signaled that action on climate change will be crucial to its support of a budget, including eliminating tax breaks for energy companies. Its budget wish-list also includes more funding for postsecondary education, affordable housing and a C\$10 per hour minimum wage. The New Democrats are being squeezed by the Green Party on the left and by the Liberals on the right, who have moved to the left in opposition and have made the environment a major plank in their platform. Currently at 13-15% in the polls, and losing ground the parties on its left and right, the NDP has an incentive to find something in the budget it can live with.

Pretexts Aplenty

¶11. (SBU) If the budget passes and proves popular among voters, the Conservatives may still be tempted to call a snap vote citing obstruction by the opposition. The PM and the opposition leaders all say that they don't want an election, but Harper's Conservatives are acting as though they do. PM Harper has used the current two-week parliamentary break to commit C\$3.5 billion to eco-projects, transit, infrastructure and farm credits across the country, contingent on passage of the March 19 budget, in what seems to be a traditional gesture of pre-election largesse.

¶12. (SBU) The Conservatives are visibly revving their campaign engines. Their bill to introduce fixed election terms would be only a momentary obstacle in the way. A greater problem for the Conservatives would be the appearance of opportunism. Polls suggest that the public has not tired of minority government, although Canadians may be tired of elections. There have been three federal elections in as many years. The support level required for a majority government is about 39%-40%, and neither the Conservatives nor the Liberals are currently at this level. The Conservatives are currently polling near the 36.3% the party won in the January 23, 2006 federal election, with the

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Liberals hovering at between 30% and 34%. The Conservatives, Quebec polling numbers remain several points below the party's score in the 2006 election. However, if conditions appeared ripe, Mr. Harper could well gamble that he could change the mood once in a campaign and that his party's 2006 poll ceiling could become its new floor.

¶13. (SBU) If an election is called, all legislation currently in progress in Parliament will die. However, much of the Conservative Party's agenda, particularly its priority justice bills, has already been effectively stalled by the opposition parties. Of the 51 bills introduced by the Harper government, only 16 have received Royal Assent. Ten of the twelve justice bills that make up the government's tough-on-crime agenda have yet to be passed, including C-10 on mandatory minimum sentences for firearms offences, one of the first justice bills to be introduced by the Harper Government and the flagship legislation of its law and order program. The bill was essentially gutted by the opposition parties in February in committee. A continued stalemate on this bill, and other anti-crime measures, could provide a pretext for an election call in which the Conservatives could tag the Liberals, particularly, as "soft on crime." For good measure, the Conservatives could add "soft on terror" based on the defeat on February 27 of Harper's motion to extend

two sunset clauses of the Anti-Terrorist Act.

¶14. (SBU) Liberal leader Stphane Dion belatedly recognized this political danger and on March 14 released a new anti-crime platform that promises more money for new prosecutors and judges, as well as for the RCMP to combat gun crimes, organized crime, gangs and drug trafficking. The package, however, has a cobbled-together feel and initial media reaction has been skeptical.

¶15. (SBU) Another trigger could come over the environment when C-30, the Clean Air Act, is reported out of committee on March 31. The Conservatives have accused the Liberals of delaying the bill. Confrontation with the Liberal Senate over S-4, a bill setting fixed terms for senators, and C-16, to allow for elections for Senate appointments, could also provide a pretext.

Comment

¶16. (SBU) The Harper government is putting in place the conditions for an election, likely sooner rather than later. Speculation revolves around a call sometime in April or early May, or even sooner if the budget is defeated, requiring an immediate dissolution of Parliament. Polls suggest that the public is in a pre-shopping mood -- interested, but not especially motivated to buy. The budget debate could change that perception. In the upcoming Quebec election, voters appear ready to replace a majority with a new minority government, adding to the uncertainty. With respect to United States priorities, election speculation is slowing meaningful progress on important bilateral issues, including IPR reform and, in the event of an election, all progress will cease in the short-term. Moreover, until the question of election timing is resolved, it will be difficult to make significant headway with distracted Parliamentarians and senior officials. That said, a majority Conservative government would likely open new lanes of bilateral cooperation that the Harper Government has to date shied away from due, in part, to its current minority status. Qfrom due, in part, to its current minority status.

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